No. 6946

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit 9

MINA H. JOHNSON, SIGMUND BEEL, and A. G. BRODIE,

Appellants,

vs.

F. E. HORTON, FRANK HORTON, JR., R. McCARTHY, A. F. PRICE, WEEPAH HORTON GOLD MINES COMPANY, a corporation organized and existing under the laws of the State of Nevada, IVEN T. JEFFRIES, O. U. PRYCE, and P. N. PETERSEN,

Appellees.

APPELLANTS' OPENING BRIEF.

MAURICE E. GIBSON,
Crocker First National Bank Building, San Francisco,
Attorney for Appellants.

Subject Index

Table of Authorities Cited

No. 6946

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

MINA H. JOHNSON, SIGMUND BEEL, and A. G. BRODIE,

Appellants,

vs.

F. E. HORTON, FRANK HORTON, JR., R. McCARTHY, A. F. PRICE, WEEPAH HORTON GOLD MINES COMPANY, a corporation organized and existing under the laws of the State of Nevada, IVEN T. JEFFRIES, O. U. PRYCE, and P. N. PETERSEN,

Appellees.

APPELLANTS' OPENING BRIEF.

STATEMENT OF FACTS.

This action was commenced in the District Court of the United States in and for the District of Nevada, in equity. Following the filing of plaintiffs' amended bill of complaint and plaintiffs' supplemental bill of complaint, both by leave of Court, defendants moved to dismiss said amended bill of complaint and supplemental bill of complaint on the following grounds:

I.

It appears upon the face of the amended bill of complaint in the above entitled cause that this suit does not really and substantially involve a dispute or controversy within the jurisdiction of this Court, because the amount in controversy does not exceed the sum of Three Thousand Dollars ($3,000.00), exclusive of interest.

II.

The jurisdictional averment of the amount involved is clearly frivolous, as the amended bill of complaint shows that the matter in controversy is title to corporate offices, and that the same is not reducible to a money valuation.

III.

That said amended bill of complaint fails to state facts sufficient to constitute a cause of action in favor of the plaintiffs and against these defendants or either of them.

IV.

The amended bill of complaint does not state facts sufficient to constitute a valid cause of action in equity against these defendants or either of them.

V.

It appears on the face of said amended bill of complaint that said amended bill of complaint is wholly without equity.

VI.

The amended bill of complaint expressly shows that plaintiff, Mina H. Johnson, has no title to maintain this suit or to any relief against these defendants or either of them by reason of the facts herein alleged, in that it appears from said amended bill of complaint that any stock held by said Mina H. Johnson at the date of the corporate meeting therein mentioned was held by her as an executrix of the Estate of I. H. Johnson, deceased.

which motion was granted by the Court. (Trans. page 49-50.) This is an appeal by plaintiffs from said order of dismissal. (Trans. pages 42-43.)

The facts as stated in plaintiffs' amended bill of complaint are substantially as follows:

Defendant Weepah Horton Gold Mines Company is a corporation organized and existing under the laws of the State of Nevada. True copies of its articles of incorporation and by-laws, as the same existed at all times referred to in plaintiffs' amended bill of complaint and supplemental bill of complaint (other than the purported amendment to said by-laws hereinafter referred to), are appended as exhibits to said amended bill of complaint and incorporated therein by reference. Neither said articles of incorporation nor said by-laws contain any limitation upon the right of the stockholders of said corporation to vote their stock in stockholders' meetings.

On the 22nd day of May, 1929, the then board of directors of said corporation adopted a resolution assessing the stock of the corporation in accordance

with the powers vested in it; and at a subsequent meeting of the board of directors of said corporation held on March 15th, 1932, the then board of directors of said corporation, consisting of defendant F. E. Horton, defendant Frank Horton, Jr., defendant R. McCarthy, defendant A. F. Price, and George C. Keough, adopted a resolution providing that the stock on which said assessment had not been paid on or before April 18th, 1932, would be sold on said last mentioned date; and at said time likewise authorized the payment of defendant F. E. Horton's said stock assessment by crediting him with certain advances alleged to have been made by him for the corporation.

There having been no stockholders' meeting of said corporation for the election of directors since on or about the 1st day of February, 1929, plaintiffs Mina H. Johnson, and A. G. Brodie and other persons, (other than the defendants) all of whom were stockholders in said corporation, jointly called a special meeting of the stockholders of said corporation in accordance with said by-laws for the purpose of electing directors of the corporation for the ensuing year, said meeting being noticed to be held at the office of the corporation in Reno, Nevada, on the 21st day of March, 1932.

At a meeting of the board of directors of said corporation held on March 19th, 1932, consisting solely of defendant F. E. Horton, defendant Frank Horton, Jr., defendant R. McCarthy, defendant A. F. Price, and George C. Keough, a resolution was adopted by said board of directors purporting to change and amend Section 4 of Article 2 of the by-

laws of said corporation by adding the following thereto:

> "No stockholder shall be entitled to vote any shares of stock on which share or shares of stock the or any assessment thereon be due, unpaid, or delinquent, and no shares shall be voted at any meeting of stockholders for the election of directors unless all calls and assessments thereon or against said stock shall be paid on the date and at and prior to the meeting of the shareholders.
>
> At all meetings of stockholders, in order to constitute a quorum, only shareholders who have paid all calls and assessments theretofore levied, shall be considered as shareholders of the company."

Said special meeting of the stockholders for the election of directors was duly held on March 21st, 1932, there being present at said meeting in person and by proxy 1,136,140 shares of the capital stock of said corporation out of a total of 1,168,300 shares of the corporation's stock issued and outstanding, At said meeting defendant F. E. Horton, defendant Frank Horton, Jr., defendant R. McCarthy and plaintiff Mina H. Johnson, plaintiff A. G. Brodie, and plaintiff Sigmund Beel were the only nominees to fill the five directorships. At said meeting 1,021,750 cumulated votes were cast for plaintiffs Mina H. Johnson, A. G. Brodie and Sigmund Beel for directors in said corporation and 774,223 cumulated votes were cast for defendants F. E. Horton, Frank Horton, Jr., and R. McCarthy for directors in said corporation. All but 142,083⅓ votes out of said 1,021,750 votes cast for said three plaintiffs were dis-

regarded and not counted in said election by the inspectors of election appointed by defendant F. E. Horton, who acted as chairman of said meeting, for the alleged reason that said purported amendment to the by-laws disfranchised stock on which said assessment at said time had not been paid. Thereupon defendant F. E. Horton announced that defendants F. E. Horton, Frank Horton, Jr., and R. McCarthy had been elected directors of said corporation and that the two remaining places on said board of directors were vacant.

Plaintiffs Mina H. Johnson, A. G. Brodie, and Sigmund Beel, refusing to accede to this ruling of the chair, and considering that plaintiffs had been elected directors, held the organization meeting of said board of directors immediately after the adjournment of said stockholders' meeting in conformity with Article 5, Section 10 of said by-laws, after announcing to the stockholders' meeting as it was adjourning, that said meeting would be so held; and at said meeting said three plaintiffs being present and acting as directors in said corporation, elected the following officers of said corporation: plaintiff Mina H. Johnson, president; plaintiff Sigmund Beel, vice-president; and plaintiff A. G. Brodie, secretary-treasurer, to serve as such until the election and qualification of their successors in office.

Following said stockholders' meeting defendant F. E. Horton, Frank Horton, Jr., and R. McCarthy purported and are now purporting to act as the board of directors of said corporation to the exclusion of plaintiffs herein and defendants F. E. Hor-

ton, A. E. Price, and R. McCarthy are purporting to act as the president, vice-president, and secretary-treasurer of said corporation, and have retained possession of the books, records, properties, and assets of said corporation and have at all times refused on demand to deliver the same to plaintiffs.

The additional facts stated in the supplemental bill of complaint are substantially as follows:

A special meeting of the three plaintiffs herein as a lawful quorum of the board of directors of said corporation was held on the 16th day of April, 1932, after due notice thereof had been sent by plaintiff A. G. Brodie, acting as secretary, to defendants F. E. Horton, Frank Horton, Jr., and R. McCarthy. At said meeting, which was not attended by any of said defendants, a resolution was adopted by the affirmative vote of all three of said plaintiffs, acting as directors, extending, for a period of ninety days from and after April 18th, 1932, the sale date for said delinquent stock assessments; and notice of this postponement of said sale date, by said plaintiffs acting as the board of directors of said corporation, was given to all defendants prior to 10:00 o'clock A. M. on the 18th day of April, 1932. Notwithstanding this notice of postponement defendants F. E. Horton and Iven T. Jeffries proceeded in the name of the corporation at 10:00 o'clock A. M. on said 18th day of April, 1932, to sell all stock of the company on which said assessment had not been paid at said time. At said sale defendant O. U. Pryce, with notice of said postponement of said sale, purported to buy two thousand shares of said stock; and at said

sale defendant P. N. Petersen, with notice of said postponement, purported to buy three hundred ninety-three thousand shares of said stock, which included one hundred eighty-three thousand shares of said stock of said plaintiffs; and at said sale five hundred forty-three thousand four hundred and ten shares of the stock of said corporation were purported at said time to be retired to the treasury of said corporation.

Based on the foregoing allegations in the amended bill of complaint and supplemental bill of complaint plaintiffs prayed for the relief set forth in the prayers in its amended bill and supplemental bill and the Honorable District Court on motion of appellees' counsel dismissed both bills for want of equity.

ANALYSIS OF FACTS OF CASE.

The important facts of the case can be grouped into two divisions:

(1) At the stockholders' meeting on March 21st, 1932, plaintiffs received the three highest numbers of votes cast for directors and consequently were elected directors of said corporation and defendants F. E. Horton, Frank Horton, Jr., and R. McCarthy received the three lowest numbers of votes cast for the election of the five authorized directors in said corporation, unless said purported amendment to the by-laws of defendant corporation disfranchising stock having unpaid assessments thereon at the time of such meeting was effectual to accomplish such disfranchisement.

(2) If plaintiffs were elected directors at the stockholders' meeting on March 21st, 1932, their action qua directors in the directors' meeting duly noticed and held on the 16th day of April, 1932, at which they extended the sale date for delinquent stock assessments was a valid corporate act binding on the agents of the corporation and those who purchased at the assessment sale with notice thereof.

It is submitted, therefore, that the appeal involves merely two questions of law, viz.:

(1) Does the purported amendment by its directors of the by-laws of a corporation, organized under the laws of the State of Nevada, purporting to disfranchise stock on which an assessment is delinquent, prevent said stock from being voted at a stockholder meeting of said corporation, there being nothing in the articles of incorporation or by-laws of said corporation in derogation of the right of all outstanding stock to be voted at such meetings and the by-laws merely giving the directors the right to amend the by-laws?

(2) Does a bill of complaint state a cause of action in equity, which

(a) Sets forth in substance that a minority of the stockholders of a Nevada corporation have attempted by an illegal and ineffectual by-law, adopted by themselves as directors, to prevent the majority of the stockholders of said corporation from electing a controlling number of its directors, and

(b) Which sets forth that certain defendants purporting to act as officers of the corporation have pur-

ported to sell to third parties, with notice, and retire to the treasury 543,410 shares of the outstanding stock of the corporation, including the stock of the plaintiffs, in contravention of a postponement of the sale date of said stock by a quorum of its *de jure* directors by resolution in a directors' meeting properly noticed and held, and

(c) Which states that certain of the defendants who were not *de jure* officers or directors are purporting to act as the sole officers and the sole directors of said corporation and are carrying on the business of the corporation and withholding its property, books, assets, and records from its *de jure* officers and directors, and

(d) Which prays for a receiver; an injunction against their so acting; the delivery of the property, books, and assets of said corporation to said receiver; the expunging of said illegal by-law from the by-laws of the corporation; the adjudication that plaintiffs are *de jure* directors and officers, and that the defendants, acting as such are not; the removing of the cloud on the title to the stock purported to have been sold by certain of said defendants for said delinquent assessments; and for such further relief as to the Court seems proper?

Appellants contend:

(1) That the purported amendment to the by-laws was null and void and of no effect at the stockholders' meeting; that consequently plaintiffs were elected directors at said meeting and now constitute three of the five authorized directors of said corporation; and

that by virtue of the proceedings taken by them at the organization meeting, plaintiffs were elected respectively president, vice-president, and secretary-treasurer of said corporation and now are its *de jure* officers, and

(2) That said amended bill of complaint and supplemental bill of complaint state a cause of action in equity, for the reason that their remedy at law is neither plain, adequate, nor complete.

(3) That the Honorable District Court erred in dismissing the amended bill of complaint and supplemental bill of complaint.

Before considering the foregoing two main points of this brief it is desirable to comment briefly on two objections to the amended bill of complaint and supplemental bill of complaint made by appellees on their motions to dismiss, to-wit:

1. That it does not appear the value of the matter in dispute is in excess of $3000.00, and

2. That plaintiff Mina H. Johnson has no title to maintain this suit.

Plaintiffs have alleged that the value of the mining claims owned by the corporation in the State of Nevada is in excess of $3000.00, and that the matter in controversy, exclusive of interest and costs, exceeds the sum of $3000.00. (Paragraphs 1 and 9, amended bill of complaint; Trans. page 2.)

For the purpose of the jurisdictional prerequisite as to the amount in controversy the value of the entire corporate assets is deemed to be involved in an action of this character and the foregoing allega-

tions as to the amount in controversy are sufficient for the purposes.

Klein v. Wilson & Co., 7 Fed. (2nd) 772;
Local No. 7 Bricklayers' Union v. Brown, 278 Fed. Rep. 271;
Presto-Lite Company v. Bournonville et ux., 260 Fed. Rep. 440.

With respect to complying with Equity Rule 27, it need only be observed that this is not a stockholders' bill. The relief sought is based on plaintiffs' rights as directors and officers of the corporation as the representatives of a majority of the stockholders of the corporation.

I.

THE PURPORTED AMENDMENT TO THE BY-LAWS WAS NULL AND VOID AND OF NO EFFECT.

All stockholders in Nevada corporations have the right to vote their stock in stockholder meetings unless the articles of incorporation provide otherwise. On this point Section 28 of Nevada Corporation Act provides:

> "Unless otherwise provided in the *certificate* or *articles of incorporation,* or an *amendment thereof,* every stockholder of record of a corporation shall be entitled at each meeting of stockholders thereof to one vote for each share of stock standing in his name on the books of the corporation";

and

Section 30 of said act provides for cumulative voting for directors when authorized by the articles of incorporation, as in the instant case.

The articles of incorporation of defendant corporation contain no limitation on the right of stockholders in the corporation to vote the stock standing in their names.

The attempt by defendants to amend the by-laws of defendant corporation to prohibit holders of stock on which assessments were delinquent from voting such stock at stockholders' meetings was a nullity and void act because of being in contravention of Section 8, subdivision 6, of Nevada Corporation Act, which provides as follows:

> "Sec. 8. Every corporation, by virtue of its existence as such, shall have power:
>
> "6. To make laws *not inconsistent* with the constitution or laws of the United States, *or of this state,* for the management, regulation and government of its affairs and property, the transfer of its stock, the transaction of its business, and the calling and holding of meetings of its stockholders."

Lilylands Canal & Reservoir Co. v. Wood (Colo.), 136 Pac. Rep. 1026;

Peoples' Home Savings Bank v. Superior Court, 104 Cal. 649, 38 Pac. Rep. 452, 43 Am. St. Rep. 147, 29 L. R. A. 844;

Brewster v. Hartley, 37 Cal. 15, 99 Am. Dec. 237;

Fletcher on Corporations, Vol. 1, Sec. 29,

wherein it is stated:

> "In order to be valid by-laws must be consistent with the law of the land. Accordingly a by-law is void if it is in contravention of any provision of the Federal or State Constitution, or of any Federal or State Statute."

The non-payment of an assessment does not affect a stockholder's right to vote prior to the sale of the delinquent stock.

Nevada Corporation Act, Sec. 74;
14 *Corpus Juris* 902, Sec. 1392.

II.

THE AMENDED BILL OF COMPLAINT AND SUPPLEMENTAL BILL OF COMPLAINT STATE A CAUSE OF ACTION IN EQUITY.

Appellees have taken the position that plaintiffs' case presents merely a question as to the title to corporate offices; that, for this reason no question of equitable cognizance or jurisdiction is presented and that appellants should be relegated to a Court of law, there to *sue in quo warranto* to determine the same. Appellants cannot concur in this attempted narrowing of the propositions confronting the Court. Something more than the mere title to corporate offices is involved in this case. In substance the question is whether the defendant corporation is to be run and managed by the selected representatives of a majority of the stockholders as provided by the laws of the state of incorporation, or whether a minority group will be permitted to maintain and perpetuate itself in office and in control of the corporation in absolute contravention to the express laws of the State of Nevada.

If appellants should be denied equitable relief the appellees would be free to run the corporation, formulate its policies, issue stock, execute contracts, incur

indebtedness, and in general to conduct the affairs of the corporation, while the appellants and the majority of stockholders would be compelled helplessly to stand by impotent to interfere with the usurpation of control by the minority until such time as a Court of law, through successive appeals perhaps, had determined merely the bare title to office. Appellees argued in the lower Court that a Court of equity was thus closely confined and their motion for the dismissal of plaintiffs' amended bill and supplemental bill was granted on that narrow ground.

We do not concur in appellees' view of the scope of equity jurisdiction as applied to the present situation. We submit that the determination of the respective titles to office is only one of the questions involved, as a reading of the amended bill and supplemental bill and the relief prayed for therein will disclose. A statement of the Court in *Westside Hospital v. Steele*, 124 Ill. App. 534, expresses appellants' views in the matter:

> "It is urged on behalf of appellants that the main, if not the only, question presented by the bill of complaint is the validity of the election of the president and treasurer of the corporation at the directors' meeting of January 10, 1906; and that a court of equity will not entertain jurisdiction of a suit, the purpose of which is merely to test the legality of the election or the removal of officers of a corporation. As to the principle of law involved in this contention we have no dissent to express—we cannot, however, agree with counsel in their statement of the case presented by the bill. As we view it, the case stated in the bill is not merely one involving the va-

lidity of an election of officers, but it involves the rights of minority stockholders of the corporation under the constitution and laws of this state to have an annual meeting of directors held according to law, and to cumulate their votes at such an election; and that the officers and management of the corporation shall only be installed in control of the corporation and its property and business, by, through, and in compliance with the law, and the legal by-laws of the corporation. The minority stockholders of a corporation have property rights in the corporation and its assets and management, which the directors, their trustees, may not ignore and set aside, nor can the majority of the stockholders, broad as their powers are, override the organic law of the corporation for the illegal purpose of preventing the minority from securing the representation in the directory which the shares of stock owned by them enable them to elect.

"The acts of the defendants to the bill resulted in putting the business and property and funds of the corporation in the hands of men who are not legally entitled to act for the corporation. The contention of appellants is that there is an adequate remedy at law for the situation shown in the bill, by quo warranto. We do not think so. As said in Bartlett v. Gates, 118 Fed. Rep. 66: 'The stockholders of this corporation are legally entitled to have a meeting of stockholders called, at which they can express their choice for directors of the company. The complainants' remedy at law is not adequate. The remedy at law would leave the parties free to renew the contest on the same and other like lines that have thus far stifled the voice of the stockholders.' See also Dodge v. Woolsey, 59 U. S. 331."

The case of *Johnstone v. Jones,* 23 N. J. Eq. 216, involved a secret stockholders' meeting. In that case the Court said:

> "If a dissatisfied director of one of our large railroad corporations could persuade a town meeting to elect new directors of his company, or was to assemble on such day as he chose to name two of its stockholders, and persuade them to vote on the whole stock of the company instead of twenty shares held by them, for himself and his associates on the ticket named by him, and they were to meet, elect officers, produce and adopt books and attempt to seize by force the road and its equipment they would be as much officers de facto and de jure as these defendants. No one would contend that a court of equity could not restrain, by injunction, such raids as these, but is obliged to leave the corporation and its lawful directors to the remedy at law, always taking at least months and in the meantime suffer the road to be operated and perhaps ruined by the depredators, because they claim to be directors de facto or de jure. A court of equity that could hesitate in such a case would be of little use."

The rule is undoubtedly correctly stated in *Fletcher Cyc. Corporations,* Vol. 5, Sec. 2070, commencing at page 234, as follows:

> "On general principles, a court of equity has no jurisdiction to determine as a principal object of the bill the illegality of an election and remove or seat officers, when there is an adequate remedy by quo warranto, mandamus, or under a statute, unless such jurisdiction has been conferred by statute. A court of equity, however, has jurisdiction to inquire into the validity of an election,

and to declare it void, when necessary to the complete adjudication of a cause over which it has jurisdiction on independent grounds, as where an injunction is necessary to prevent waste or misappropriation of the corporation funds or destruction of the corporate business, or unwarranted interference with its management and business affairs to its manifest detriment, or where a fraud is being perpetrated and cannot be prevented except by a court of equity, or where there has been a breach of trust, or where an accounting is proper, or where property rights and incidentally office rights are involved," etc.

There is no controlling statute in the instant case. It is submitted, however, that the instant case brings itself within some of the foregoing exceptions noted by Fletcher, for the reasons that:

1. The action of the defendants as a minority group in attempting to perpetuate themselves in office by means of an illegal by-law adopted by them two days before the stockholder meeting in question constituted and continues to constitute a fraud on the majority stockholders of the corporation giving an independent ground for equity jurisdiction.

Humboldt Driving Park Assn. v. Stevens, 34 Neb. 528, 52 N. W. 568, 33 Am. St. Rep. 654;
Johnstone v. Jones, supra;
Westside Hospital of Chicago v. Steele, supra;
Schmidt v. Pritchard, 135 Iowa 240, 112 N. W. 801;
Singer Mfg. Co. v. Yarger (C. C. Iowa, 1880), 12 Fed. 487;
Walker v. Johnson, 17 App. (D. C.) 144;
Hughes Fed. Practice, Vol. 2, Sec. 960.

2. The expunging of the illegal by-law from the by-laws of the corporation is an independent ground of equity jurisdiction.

Lutz v. Webster, 249 Pa. 226, 94 Atl. 834;
Westside Hospital of Chicago v. Steele, supra.

3. The right of a corporation through its duly elected directors and officers to control and have possession of its property, records, and other assets is a valuable property right which equity will protect.

Society of Mutual Succor St. Mary of Lattini of Rocca-Monfina v. Iacobe et al., 232 Mass. 263, 122 N. E. 292;
Hughes Fed. Practice, Vol. 2, Sec. 972;
International News Service v. Associated Press (1918), 248 U. S. 215, 39 S. Ct. 68, 63 L. Ed. 211.

In addition thereto the clearing of the cloud on the stock purported to have been sold for delinquent assessments is a matter of independent jurisdiction in equity.

Hughes Fed. Practice, Vol. 2, Sec. 974;
Shaniwald v. Lewis, 5 Fed. 510 (District Court Nevada 1880).

4. The appointment of a receiver for the assets of a corporation and the issuance of an injunction are still further grounds for independent jurisdiction in equity.

Hughes Fed. Practice, Vol. 2, Secs. 1027, 1028 and 1142.

The true equity rule is thus laid down by Story's Equity Jurisprudence (Sec. 33):

> "The remedy must be plain, for, if it be doubtful and obscure at law, equity will assert a jurisdiction. It must be adequate, for, if at law it fall short of what the party is entitled to, that founds a jurisdiction in equity. And it must be complete; that is, it must attain the full end and justice of the case. It must reach the whole mischief, and secure the whole right of the party, in a perfect manner, at the present time, and in future; otherwise equity will interfere, and give such relief and aid as the exigency of the particular case may require."

Tested in the light of this definition the remedy at law in the case at bar would fall short of measuring up to this rule, for such a remedy would be neither plain, adequate, nor complete.

For these reasons it is respectfully submitted that the judgment of the Honorable District Court should be reversed.

Dated, San Francisco,
December 23, 1932.

Respectfully submitted,
MAURICE E. GIBSON,
Attorney for Appellants.